THE NATIONAL CITY BANK OF NEW YORK

1932

Economic Conditions
Governmental Finance
United States Securities

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General Business Conditions

THE chief influence on business sentiment during the past month must be looked for in the political rather than the trade news, for undoubtedly the campaign has been the topic of absorbing interest. Partisan feeling has been on the increase; and in the campaign speeches the history of the depression and the record of each party have been raked over in a manner sometimes disturbing, and tending to obscure the important fact that both parties have taken the conservative side of the major issues.

What the country needs from both parties is determination to preserve sound principles in public finance. The central element in such a program must be the balancing of budgets through reduction of expenditure. There are honest differences of opinion as to the ability or resolution with which one party or the other will carry out this program, and these differences are exaggerated by partisan feeling, and promote uncertainty. But there is no basis for prejudgment or anxiety. It is rather to be considered that the most notable aspect of this campaign is the endorsement by both candidates and party platforms of principles of economy and sound money. They are alike in recognizing the importance of balancing the budget, and there is no agitation of the money question among the leaders of chief influence within either party.

It is to be recognized that the influence of the depression has been towards conservatism. Amid all the distress common sense has prevailed. Economic panaceas of unsound character have been offered in multitude, but they have found little foothold. Only one proposal in any degree threatening the soundness of the money has made even slight headway, and this, the bonus, passed but one house of Congress and if it should some time pass the other unquestionably would receive the Presidential veto. Efforts to stir up one group of the population against another are no more in evidence than in good times, since it is obvious that all groups are suffering much alike.

Since early July there has been a vigorous and impressive business improvement, and the country very well understands that this recovery followed upon the relief of fears concerning the dollar and the financial situation generally, just as the collapse of business in the Spring was a consequence of those fears. This demonstration of cause and effect has been a convincing one, and wins support for sound policies. Another reason why the demand for economy and sound public finance has continuously grown is the increase in the tax burden, now that taxes must be paid out of incomes cut in half.

Pertinent to the foregoing is the following extract from the bulletin on the agricultural situation published by the Corn Belt Farm Dailies, under date of September 30:

> It would be a wonderful thing if both candidates could spend a little more time with practical farmers and a little less with political farm "leaders." They would discover, for one thing, that the most effective vote-getting talk at the present time would be along the line of cutting down bureaucratic activities of the government and reducing costs and taxes, and not the promotion of schemes to involve the government in nobody knows how many millions or hundreds of millions of new expenses, and business in costly uncertainties of world-wide influence.

This is not quoted as a criticism of the candidates, but as informed testimony to the state of mind which is entering into the elections this year in the farm country, and, it is safe to say, elsewhere also. The evidence is convincing that the sentiment of the country is for economy, and for a balance between receipts and expenditures that will keep the public credit above reproach. The political history of the country justifies the utmost confidence that any Congress elected will contain a majority supporting these principles.

The Treasury and the Money Market

Of course some people still believe that the way out of the depression is through the expenditure of government credit in gigantic sums. They interpret the subscription to the offering of $450,000,000 Treasury notes on October 15, which was oversubscribed eighteen times, as evidence of an almost unlimited

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ability of the Treasury to borrow. However, this is a serious misapprehension. Aside from the familiar "padding," due to institutions subscribing for more notes than they expected to get in order to get all they wanted, the oversubscription reflects an unnatural and undesirable condition in the money markets, growing out of the depression. Capital shuns investment in private enterprises of all but the highest credit, and indeed avoids commitment in long term obligations of any sort. Thus there is a great piling up of funds in the money centers seeking liquid short term investments of high standing, among which the Treasury notes and certificates are of course pre-eminent. These are funds normally needed by business, and they will be needed again as business recovers. Their diversion to Treasury uses is not a sign of the strength of the public credit, but of the weakness of business.

Moreover, the banks are in funds by reason of the large volume of Federal Reserve Bank credit outstanding, and short term government securities provide the only important outlet for the investment of their excess reserves. This is the chief explanation for the oversubscription mentioned.

The questions involved in government credit policies in the depression are complex ones, and people may sincerely differ upon them. However, two propositions seem indisputable. First, there are plainly limits beyond which the government debt cannot be expanded without causing such alarm as to offset, and perhaps more than offset, the temporarily stimulating effect of the disbursements. There is no gain from employing the national credit to replace private capital in support of business if the policy drives as much or more private capital out of business, into government obligations, into hiding, or even out of the country.

The second proposition is that the public credit cannot be employed continuously to support the economic organization unless it is preserved by a balanced budget. The government, like an individual, must in the long run live within its income; otherwise its credit will decline. During the fiscal year to date, (October figures up to the 22nd) the current operating deficit was $601,000,000, and if the $345,000,000 allotted to the Reconstruction Finance Corporation be added the total was $946,000,000. For the same period of the preceding fiscal year the operating deficit was $635,000,000.

Consideration of these figures must, of course, take account both of the fact that the new income rates do not become effective until after the first of the calendar year, and also the fact that internal revenue receipts in the early months of the fiscal year were undoubtedly diminished by the tendency of purchasers to anticipate their needs before the new taxes went into effect. The yield of these taxes has lately been increasing. Moreover, any improvement of business would further lessen the demands on the Reconstruction Finance Corporation, as well as speed up the repayment of its advances. All of which would tend to improve the Treasury position. However, none of this is certain. Since this is so the country cannot afford to ignore the import of the current figures, nor abate its determination to bring the budget to a balance.

The Business Recovery

The gains in business activity have been well maintained during October, and in general a hopeful attitude prevails for which there is warrant in the impressive demonstration of recuperative power given within the past three months. In July the long decline of business was checked, in August there was a substantial upturn, in September a greater rise, and in the first part of October most of the common measures of business activity for which figures are available continued to advance. The gain in car loadings, extending later into the Autumn than usual, is notable, and includes nearly all classifications of freight.

In part the business recovery has been seasonal, but in extent it has been more than seasonal, and all the composite indexes of business volume which are adjusted for the seasonal factor have turned up more sharply than at any time since the long decline began. The following table gives the index compiled by the Annalist, showing all its components, the advances in each instance being over and above the ordinary seasonal rise:

Annalist Index of Business Activity
(Estimated Normal = 100)

	July	Aug.	Sept.	Percent Change July to Sept.
Pig Iron Production	18.0	16.7	19.7	+ 9.4
Steel Ingot Production	19.3	18.3	22.5	+16.6
Freight Car Loadings	48.8	48.9	52.4	+ 7.4
Electric Power Production	67.3	67.5	68.0*	+ 1.0
Bituminous Coal Production	45.1	49.9	57.0	+26.3
Automobile Production	32.3	24.6	25.4	—21.4
Cotton Consumption	57.4	75.3	89.0	+55.1
Wool Consumption	65.1	87.1	96.4*	+48.1
Boot and Shoe Production	83.4	91.0	92.5*	+10.9
Zinc Production	31.2	27.8	27.6	—11.5
COMBINED INDEX	52.0	55.5	59.9*	+15.2

* Preliminary

These figures support the common observation that the rise in textiles has been the most pronounced, and the showing would be still more striking if silk and rayon consumption were included. Following their record sales in August, the cotton mills had a satisfactory September and sold slightly more than their production for the month. Cotton consumption increased from the low of 279,000 bales in July to 492,000 in September. Wool consumption in May was only 16,500,000 pounds, but was 42,000,000 in August and is estimated

around 46,500,000 in September. Mill takings of raw silk rose from 33,000 in May to approximately 60,000 each in August and September. Rayon operations climbed in the same period from an estimated 15 to 20 per cent of capacity to 100 per cent.

Of course, this great expansion, which extended to the apparel lines including shoes and furnishings, covered needs ahead. Therefore October has been a dull month in the primary markets. However, reports of retail trade, which must support this improvement if it is to be held, are likewise better. In the first half of October department store dollar sales in metropolitan New York were only 13.9 per cent off from last year.

The Heavy Industries and Employment

The rise in steel output shown in the foregoing table is less impressive in tonnage than in percentage, the actual gain in operations having been from 13 to 19½ per cent of capacity. Automobile output has declined during the period. The industry is cleaning up stocks in preparation for new models, on which production will be under way within the month. Meanwhile the seasonal drop in sales has been less than usual.

Awards of building contracts, running only one-half of last year's totals, nevertheless indicate a bottom. The third quarter was better than the second, contrary to the usual seasonal movement. The rise in lumber orders has been substantial, and gives evidence of delayed repair work finally undertaken.

These reports indicate that the improvement, while irregular, has been well distributed, and further confirmation occurs in the employment figures of the Bureau of Labor Statistics. In September there was a rise of 3.6 per cent in industrial employment, and payrolls rose 2.6 per cent. Both are larger than the usual seasonal gains, and twelve out of fourteen groups showed increases. However, the number put back to work is distressingly small as compared with the total of unemployed. In his Detroit speech President Hoover, citing the Department of Commerce as his authority, gave the number of those returned to work in the manufacturing industries as 180,000 in August, 360,000 in September, and more in October. As some of this gain represents only seasonal resumptions, the figures should warn against any tendency to overemphasize the improvement or to expect too much in the way of increased purchasing power this Winter.

Commodity Prices Reactionary

The truly disappointing feature of the business situation is the downward movement of commodity prices, which has continued since early September. Great importance was correctly attached to the Summer rise, which not only added to purchasing power in the farm market, where it was badly needed, but gave a new incentive and stimulus to trade. However, the rise was too great to last. Wheat has lately sold 16 cents and corn 12 cents below the top, and both at new lows for the depression. Cotton has lost 3 cents of its 4 cent advance, and hogs the greater part of their early Summer gain. Cattle and hides, wool and other farm products with some exceptions have reacted, and the non-ferrous metals also are lower. Among the imported products, representing purchasing power in other countries, cocoa, rubber, coffee and silk have dropped much of their advance.

In the security markets also the trend during October has been reactionary, and probably the influences at work are the same in all the markets. It would be interesting to know what those who were saying in August that the rise in stocks and commodities was engineered for political purposes are saying now. The outcome proves the truth of the statement made in this Letter two months ago, that the buying came from the plainest of motives, i.e., the buyers believed they would make money, and that no other explanation was correct or necessary.

It may be considered that the price reaction reflects in mercantile circles a disposition to estimate trade prospects conservatively, and in business sentiment generally a recognition of uncertainties and difficulties that hamper recovery. The disturbance of international trade and finance is a continuing factor, and there has been a fresh disturbance in the month in a further decline in the pound sterling, which affects other currencies, introduces new elements of competition and uncertainty, and is an unfavorable influence on prices everywhere. It is evident that a "managed" currency, cut loose from gold, may prove unmanageable, and of course the fluctuations are unsettling.

Still more important is the evidence given by the price decline that within this country the relationships of prices continue out of balance. The lack of a fair relationship between various prices is a factor depressing all prices, since it destroys the fair exchange value of the different commodities and manufactured goods, reduces purchasing power, throws people out of work, and so on in the familiar sequence. Per contra, progress toward restoring fair price relationships adds to the exchangeability of goods, increases purchasing power, and the influence moves around the circle in the other direction, with the effect of raising the prices which are out of line. The drop in prices of what the farmers and raw material producers sell again warns of the necessity of reducing the prices of what they

buy if the present improvement is to be turned into lasting recovery.

Though anyone can cite places in which further adjustments seem imperative, cost reduction is continuously making progress. The decrease in the price of steel rails from $43 to $40 a ton is a change that has been considered essential. The monthly reports of the Labor Department cite numerous cuts in wage scales, there having been 500 in the month ended August 15. Each of these is a step toward giving more employment. The coal miners in the central field have had more work as a result of the wage reductions they have accepted.

Two factors opposed to further drop in prices and affording hope of improvement may be considered. There is no financial pressure causing the renewed decline, for the improvement in credit conditions has continued; and without financial pressure there seems no reason for prices to seek the former bottoms. Moreover, the statistical position of some commodities is improved, and in almost none is it weaker. The supply of cotton in the country is about 2,500,000 bales less than one year ago, and exports and consumption are larger.

Money and Banking

The banking situation continues to manifest the improvement which has been one of the most encouraging features of the recovery of business to date. This improvement is the result principally of a decline in the domestic hoarding of currency and the return of gold from abroad.

During the first two weeks of October there was an increase in currency outstanding, due to regular first-of-the-month payroll requirements and Columbus Day holiday demands. Succeeding weeks, however, brought the total down to a new low point since June, off $191,000,000 since early in July when the combination of July 4 holiday requirements and banking difficulties at Chicago carried the total circulation to an all-time peak. The fact that the decline since mid-Summer has occurred in the face of a considerable pick-up in employment and retail trade, which would naturally call for more currency, is an indication that substantial sums have come out of hiding.

In addition to the return of currency, banks have gained funds through receipts of gold from abroad which totalled $67,000,000 during October and brought the net gain of gold since the June low point to $349,000,000. As a result, member bank reserves have increased approximately $300,00,000 in the past four months, and are back almost to where they were before the commencement of the panic in September a year ago. Member bank borrowing from the Reserve Banks has been reduced to pre-panic levels, and the excess of reserves above legal requirements has piled up to new high levels, above $400,000,000.

A falling off in the number of bank failures and bank applications for help from the R. F. C. are among other indications of improved conditions in recent months. The following table showing bank failures and reopenings by months, together with bank borrowings and repayments of R. F. C. funds, is indicative of the more favorable trend recently:

1932	No. of Bank Failures	No. of Re-openings	Loans to Banks by R.F.C.	Repayments by Banks to R.F.C.
Jan.	342	19	....	....
Feb.	121	43		
Mar.	47	38	$125,417,141	$6,249,542
Apr.	74	22		
May	82	23	371,970,795	62,124,401
June	151	21		
July	132	24	104,178,129	34,803,195
Aug.	85	25	77,631,277	28,815,867
Sept.	65	14	27,394,443	30,724,106
Oct. 1-27	65	16	....	....

Do We Need *More* Currency?

The significance of the figures quoted is that funds are extremely plentiful in this country, and it remains only to find suitable avenues of investment. The present large store of unused bank credit is in flat contradiction of the claim advanced by some that there is a shortage of money to finance business, and that there must be large issues of currency to restore prosperity. Business in this country, as has been pointed out before, is not financed with currency, except in the case of small retail purchases. It is financed with bank credit, and bank deposits are the money in which 90 per cent of all trade is settled. The important thing to the business of the country is that the credit-making capacity of the banking system should be equal to the demands likely to be made upon it, and of this there can be no doubt in view of the huge surplus of bank reserves already referred to.

The fact that currency which has been outstanding is now flowing back to the banks is proof that business has all and more currency than it needs. Moreover, the reduction in the total outstanding has occurred despite the issuance of some $120,000,000 of new national bank notes since the passage of the Home Loan Bank Bill in July. The market has refused to absorb additional currency, with the result that the putting into circulation of additional national bank notes has simply pushed a corresponding amount of Federal Reserve notes or other types of money into retirement.

What would help far more than unwanted additions to the supply of currency would be a moratorium on further proposals for tinkering with our monetary and currency system. Such proposals tend to destroy confidence and prevent the utilization of existing funds in industry and trade. The extent of improve-

ment that has taken place in the financial field and in business in the few months since the adjournment of Congress is evidence of what business can do in the way of bettering itself in a period of respite from the influences of fear and uncertainty.

Foreign Money Markets

Conditions in the chief money markets of Europe are very similar to conditions here. This is particularly true of the leading creditor countries, Great Britain, France, The Netherlands and Switzerland. Even in Berlin, where conditions a year ago were very stringent, the strain is much reduced. Following are recent figures upon short term money:

Short Term Interest Rates in Europe

(As of the middle of October)

	Call Money	3 Month Bill Rate
London	¼ to 1	¾ to ⅞
Paris	⅝	1 to 1 1/16
Amsterdam	¼	¼
Zurich	1	1½
Berlin	4½ to 5½	3⅞

The British Debt Conversion

In London the Bank of England has contributed in some degree to this state of ease by placing additional credit in the market through the purchase of securities—the same method which our Reserve banks practiced earlier in the year—as well as by a low discount rate. The motive in the case of the Bank of England has been particularly to aid the huge refunding operation which the British Treasury has been carrying on since the 1st of July, the conversion of £2,085,000,000 outstanding 5 per cent war loans into a 3½ per cent loan without a payment date. As a further means of favoring this operation the London market was closed for three months to all other flotations. These acts, however, although contributory to the great success of the conversion, were precautionary rather than essential. Great Britain is a country of great financial resources, and notwithstanding the bad times has a constant surplus of income for new investments. A slowing down of demands for new capital soon results in an accumulation of funds. The clearing banks as of the end of September show a decline in their advances to customers in one year of £110,000,000, while their deposits were up £153,000,000 and their deposits at the Bank of England had increased £26,000,000. This reflects slackening trade, as well as easy money.

The conversion operation accomplishes a saving to the Treasury equivalent to about £30,000,000 per year.

Since the big refunding operation was completed the Treasury has sold another issue of £150,000,000 2 per cents, due in 1938 but callable in 1935 or later. These bonds were taken at par, meeting particular favor with banks.

Of the significance of the interest rate reduction the London Times has said:

By the conversion of War Loan the British Government has set a new and higher standard of security values to which practically all other securities will sooner or later become adjusted. This is a gain of immeasurable value to all borrowers, particularly to Governments, municipalities, and corporations with large fixed-interest-bearing debts. The steep fall in wholesale commodity prices, particularly in the primary products, has enormously increased the burden of debtors, and short of repudiation they have no other means of lightening it than to replace dearer by cheaper capital. Debtors who have carefully safeguarded their credit during the period of difficulty are in the best position to take full advantage of the new investment standard which has been established by the British Government. The gain to industry and commerce will be no less marked than to Governments. It will, for instance, enable companies with dear securities to refund them on a cheaper basis, and the resultant savings would inure to the advantage of equity holders upon whom has fallen, quite properly, of course, the full weight of the depression in trade and in earnings. This, however, does not exhaust the benefits of conversion. Capital values have been restored by it to the tune of hundreds of millions, and the practical and psychological effects of this appreciation of securities, though difficult to measure, are unquestionably very great. It helps, for instance, to recreate reserves which last year had to be encroached upon to make good depreciation in securities, and to improve the balance-sheet of every company holding investments. The fact that an investor's securities are rising instead of falling predisposes him to spend and to invest afresh.

An Australian Conversion

The Commonwealth Government of Australia within the last month has refunded in the London market an outstanding issue of about £12,000,000 of New South Wales 5¾ per cent stock, maturing November 1st next, into five year 3½ per cent stock at 97½, terms which yield about 4 per cent to maturity. Under an act of the Commonwealth Parliament passed in 1929 all loans of the Australian States are guaranteed by the Commonwealth. A Labor party government of New South Wales permitted an interest payment on this loan to default some months ago, whereupon the payment was promptly made by the Commonwealth Government, and now the principal is paid off in like manner. This action cannot fail to be of lasting benefit to all Australian credit. The people of Australia have been put to a hard test in the last three years, with a large foreign debt and a heavy fall in the prices of all their export products, resulting in an appalling deficit in their foreign trade account. There were, of course, Australians—some of them in office—who talked about scaling down the payments to foreign creditors, but they were soon sent to the rear, and by an overwhelming vote the Australian people set themselves to the task of meeting their obligations. By increasing taxation, including a 6 per cent sales tax, controlling importations, drastically cutting public expenditures, reducing wages and salaries in private

business to correspond with the declining costs of living, they have met all payments, achieved a safe position in their foreign exchange account, restored the market value of their outstanding loans and established their credit as evidenced by the £12,000,000 (about $40,000,000 at present exchange rate) flotation mentioned above.

A French Conversion

The French Government also in the last two months has carried through a successful conversion operation, aggregating 86,000,000,000 francs (about $3,370,000,000), by which it retires six different issues bearing interest rates ranging from 5 to 7 per cent and substitutes a new issue, amortizable over a period of 75 years, bearing 4½ per cent.

The easy money situation in France is illustrated by the fact that the discounts and advances of the Bank of France declined from 15,011,000,000 francs at the end of December, 1931 to 5,182,000,000 at the end of September, 1932.

Obviously the large withdrawals in 1931 and 1932 by European institutions and individuals of funds employed abroad (mainly in the United States and London) have had considerable effect in easing conditions in Europe. In one of its studies, the Bank for International Settlement placed the aggregate of international short term indebtedness as of October, 1930 at 60,000,000,000 Swiss francs or $11,500,000,000, while declared foreign exchange holdings of 26 principal central banks then amounted to $2,070,000,000. Today, two years later, foreign exchange balances of practically the same countries have shrunk to $500,000,000 and the total short term indebtedness probably contracted even more in proportion. Also there has been the liquidation of a substantial amount of long term investments by certain European countries. Pierre Meynial, authority on French capital movements, estimated recently that France alone liquidated in 1931 something like Fr. 12,000,000,000 ($470,000,000) of foreign securities, chiefly American. Selling of foreign securities also explains the accumulation of abnormally large funds in Switzerland where leading Continental investment trusts are located.

In addition to the foregoing capital movements, a decline of note circulation and discounts and advances, resulting both from a decrease of hoarding and contracting trade, has been a factor in easing conditions.

The Central banks of The Netherlands, Switzerland, France and Belgium are examples of extreme liquidity. The Swiss National Bank reports that its bill portfolio at the end of September was only $3,000,000, the lowest in twenty-five years. Its gold holdings exceed note liabilities by about 67 per cent. The gold holdings of the Bank of The Netherlands exceed its total note circulation, and those of the Bank of France are approximately equal to notes in circulation. The deposit liabilities of these, as of all European banks, are comparatively small.

Even in the countries where economic conditions, on account of the low prices for agricultural products, are very difficult, official discount rates are lower. In Germany and Austria they are now as low as in pre-war years, although this by no means indicates that money is easy. The difficulty is that owing to exchange conditions there can be no free movement of capital between the banking centers, as when the gold standard was effectual.

Outlook for Cheap Money

All in all the result of the above factors has been abnormally cheap money in creditor countries. The rate at which Treasury Bills have been taken recently in the world's chief financial centers is an absolute low record, not even approached during the long period of exceptionally easy monetary conditions in the ninties of the last century.

Assuming that the worst of economic disorganization has been seen, and that gradually the severed relationships will be reformed, business resumed, confidence restored, and that idle capital will seek employment, it seems altogether probable that interest rates will be low for a protracted period.

This is taking the moderate view of probable recovery, i. e., looking for recovery in industry and trade and a reorganization of monetary systems, but without rapid recovery of speculative demands for money. It seems probable that the spirit of speculation has been tamed for some time to come, and something of the spirit of speculative adventure is required to maintain interest rates when the country is accumulating capital at a normal rate. Ordinary trade requires comparatively little credit, for trade settles itself. Money is borrowed to carry out plans for anticipating future needs and such plans may lag for a time. They are quite sure to unless interest rates are so low as to afford inducements.

Furthermore, if it be true, as the pessimists say, that the creditor class is going to absorb an undue proportion of new wealth in interest charges, it is certain that that class will have to take unusually low rates of interest in order to get its increasing wealth into employment—possibly the lowest rates ever known. that is to say, competitive conditions will determine that if the returns of capital at interest are high in comparison with the returns of capital otherwise employed, interest rates inevitably will fall until that ratio is corrected,

and it will be corrected rapidly. If no reckless monetary legislation is enacted involving the standard of value in uncertainty, existing indebtedness will be rapidly refunded at lower interest rates and a lower level of interest rates will go far to reestablish higher capital values. It was the depression of the nineties which reduced the rate of interest on new railroad bond issues to 3 per cent, and the rate on British consols to 2½ per cent; and although securities bearing these rates were not in fashion very long this was because prosperity came back so fast after 1898 that there were innumerable demands for capital at higher rates. If all prices rise, and everybody is making money again, no one will worry about debts or interest charges, but if prosperity comes back at only a slow or moderate pace the creditor class will have to accept a reduction of interest rates which will have the effect of gradually amortizing the debts. The creditor class cannot have it both ways—high interest rates along with an increment to the value of the principal. The economic law takes care of such adjustments better than legislation can do it.

The Bond Market

Chief interest in the bond market during the past month has centered in the government and municipal sections, as was to be expected in view of the widespread attention being given to Federal and local finances. The long term Treasury issues have been slightly easier, but for the short term obligations the demand has been very heavy, and without exception the U. S. Treasury notes and certificates, maturing in less than five years, have reached new highs during the month. The 4½ year 3 per cent notes sold on October 15 quickly advanced to more than one point premium and are currently quoted to yield around 2¾ per cent. A $75,110,000 issue of Treasury bills was awarded in the middle of the month on an annual interest basis of 0.14 per cent, another new low, the entire amount costing the Treasury but $26,289 for the 91 days to maturity. A subsequent issue sold at 0.20 per cent.

The reason for this great strength in short term issues is to be found in the excess bank reserves. Under present conditions, banks are placing their idle funds in securities of this class. During the four weeks ended October 19 the reporting member banks added $194,000,000 to their holdings of government securities, and undoubtedly the great bulk was in the shorter maturities.

New York City Bonds

The center of interest in the municipal market has been the situation in New York City. Following the change of administration at the beginning of September, and the vigorous measures taken at once by the acting Mayor to cut expenses, the credit of the City as measured in the price of its long term bonds sharply improved, and the 4¼s of 1981, which had sold below 80, rose above 95 in mid-September. But when the Mayor's economy plans were later overruled by the Board of Estimate, and budget schedules for 1933 were prepared which investors obviously considered as weakening the credit of the City, a slide began which carried the bonds down to about 86; and the market narrowed to a point where the offering of even a moderate amount of bonds would have caused a further severe drop.

On October 13, the request of the City Comptroller for a loan of $35,000,000 from the City's bankers, the Chase National Bank and the National City Bank, for the purpose of meeting pressing requirements, including payrolls and unemployment relief, brought the problem of the City's finances to a critical point. Following representations by these banks of the necessity of effecting economies to re-establish the City's credit as an essential preliminary to further financing, the Board of Estimate and Apportionment adopted a revision of the subway financing program, which relieved the budget of $49,750,000 charges on that account. Further accounting changes and minor cuts in expenditures were made, reducing the budget $56,242,000 below the first tentative figure, and leaving it at $558,407,000 compared with $631,366,000 in 1932, and $538,929,000 in 1929, the last year of prosperity.

These measures, however, were not regarded as adequate by the bankers, or by investors or civic organizations generally. In a letter dated October 29 to Comptroller Berry, Mr. Charles E. Mitchell for the National City Bank, and Mr. Winthrop Aldrich for the Chase National Bank, agreed for their respective institutions to finance the City's November requirements, estimated at $18,500,000 exclusive of unemployment relief. At the same time they declined to make any commitment for further financing, pending more concrete evidence of determination on the part of the City to reduce expenditures. The letter recites the previous pledges made by the City to introduce economies and points out the unsatisfactory progress made in carrying out these promises. The letter says in part:

> With respect to the budget of 1933 as it now stands, we are driven to the conclusion that a large portion of the reductions do not represent actual saving in expenditure but rather a postponement in maturity of the city's obligations or a transfer to capital account of items heretofore paid from current receipts. Reductions so made represent measures for the current relief of taxpayers, but the true savings indicated in the budget in administrative operating expenses of the city for 1933 are no more satisfying to the city at large, or specifically to those various civic bodies which in these last weeks have been giving their earnest attention to the subject of retrenchment, than

they are to your bankers and the investing public. While these reductions may not be of a character to give any warrant that the city administration is now engaged in an earnest and effective effort for financial reform, nevertheless they represent a step in the right direction which will and must be hastened by a continuing and insistent popular demand for economy.

After the receipt of this letter by the Comptroller and following a meeting of the bankers with a committee of the Board of Estimate and Apportionment on Oct. 31, Mr. Mitchell said to the press, "We have been assured of the full cooperation of the Board of Estimate and are more hopeful of the future than we have been for a long time past."

The basis of New York City's credit unquestionably is of the finest. The situation has nothing to do with that, but concerns the policies pursued. The weakness in the City's issues has been an exception in the general municipal market, which has continued strong; this is evidence that buyers judge the situation of each borrower on its own merits.

The Corporate Bond Market

The trend of corporate bond prices has been slightly downward. Most of the easing occurred in the lower grade bonds, moving in sympathy with the stock market. The high grades, influenced more directly by the ease of money, have held steady. The reporting member banks have quite substantially increased their holdings of securities other than U. S. Governments, in addition to their further purchases of government obligations. Insurance companies and savings banks have continued buying in larger volume than earlier in the year. Of course, this buying has been in the high grades.

Third Quarter Profits

Corporate earnings reports covering the third quarter, published during the past month, reflect the abnormally low rate of business activity and the difficulty of reducing manufacturing and distribution costs in the same proportion that volume has declined. A tabulation of the reports of 205 industrial companies that have been issued to date shows a combined deficit of approximately $14,000,000 for the third quarter this year, compared with a net profit of $6,000,000 in the second quarter, a profit of $25,000,000 in the first quarter and a profit of $90,000,000 in the third quarter of 1931. For the first nine months of this year the same companies showed a combined net profit of $18,000,000, compared with $364,000,000 in the corresponding period of 1931. A summary of the reports for the nine months is given in the accompanying table. In connection with the figures it should be considered that the scope of a quarterly tabulation is necessarily restricted, since a large number of companies publish only annual statements. Moreover, a large number of concerns in the "lighter industries", including textiles, clothing and shoes, as well as the smaller retail organizations, in which the recovery since the middle of the year has been centered, are privately owned and their reports are not

INDUSTRIAL CORPORATION PROFITS FOR FIRST NINE MONTHS

Net Profits Are Shown After Depreciation, Interest, Taxes, and Other Charges and Reserves, but Before Dividends.

Net Worth Includes Book Value of Outstanding Preferred and Common Stock and Surplus Account at Beginning of Each Year.

(In Thousands of Dollars)

No.	Industry	Net Profits Nine Months 1931	Net Profits Nine Months 1932	Per Cent Change	Net Worth January 1 1931	Net Worth January 1 1932	Per Cent Change	Annual Rate of Return Per Cent 1931	Annual Rate of Return Per Cent 1932
1	Autos—General Motors	$97,455	$10,555	— 89.2	$966,802	$923,803	— 4.4	13.4	1.5
9	Automobiles—Other	6,194	D-9,925	......	246,959	229,818	— 6.9	3.3	......
16	Auto Accessories	8,685	D-2,511	......	200,819	185,997	— 7.4	5.8	......
7	Baking	26,573	19,891	— 25.1	293,441	284,330	— 3.1	12.1	9.3
4	Building Materials	D-753	D-7,984	......	146,697	133,820	— 8.8	......	......
15	Chemicals	71,759	36,908	— 48.6	1,046,742	998,539	— 4.6	9.1	4.9
5	Coal Mining	1,130	D-1,551	......	95,305	92,560	— 2.9	1.6	......
7	Electrical Equipment	29,885	671	— 97.8	731,632	702,959	— 3.9	5.4	0.1
16	Food Products—Misc.	67,208	49,451	— 26.4	637,072	614,298	— 3.6	14.1	10.7
1	Iron and Steel—U. S. Steel	17,344	D-54,542	......	2,059,089	2,003,693	— 2.3	1.1	......
15	Iron and Steel—Other	D-8,773	D-48,687	......	1,539,422	1,457,500	— 5.3	......	......
6	Machinery	1,351	D-2,720	......	86,223	77,191	—10.5	2.1	......
3	Merchandising	D-2,581	D-4,902	......	171,912	149,596	—13.0	......	......
6	Mining, Non-ferrous	334	D-1,556	......	151,578	146,169	— 3.6	0.3	......
5	Paper Products	1,962	D- 287	......	70,811	70,026	— 1.1	3.7	......
14	Petroleum	D-27,612	7,435	+	1,048,547	969,372	— 7.6	......	1.0
5	Railway Equipment	6,041	1,964	— 67.5	145,841	133,018	— 8.8	5.5	2.0
5	Textiles	1,415	D-1,574	......	58,563	53,924	— 7.9	3.2	......
6	Tobacco (Cigars)	2,889	1,580	— 45.3	65,207	60,537	— 7.2	5.9	3.5
61	Miscellaneous	43,275	25,797	— 59.2	1,147,244	1,049,157	— 8.5	7.4	3.3
205	TOTAL	$363,781	$18,013	— 95.0	$10,909,906	$10,336,307	— 5.3	4.4	0.2

D—Deficit

publicly available. Without the two basic industries of steel and automobiles, which weigh heavily in the totals, the nine months' earnings of the remaining companies declined from $251,000,000 to $120,000,000, or by 52 per cent.

All of the classifications given show a decline in earnings compared with a year ago, with the exception of the petroleum industry, in which fourteen companies changed from a combined net deficit of $27,612,000 last year, when inventory losses were heavy, to a net profit of $7,435,000 this year. In considering the drastic decline in many of the other groups, a number of which show net deficits, it should be kept in mind that there is a large proportion of individual companies in various industries still operating at a profit, but offset by the losses of other companies. For example, in the third quarter of this year approximately 53 per cent of the companies reported profits, aggregating $56,000,000, but these were offset by losses of the remaining 47 per cent aggregating $70,000,000.

Although the earnings of industrial corporations, considered as a whole, were decidedly poor for the third quarter and nine months, remarkable and continuous progress has been made toward lowering of costs, without which the reports would be much worse than they actually are. Today the majority of companies are able to "break even" on a much smaller volume of business than would have been possible three years, or even one year ago.

Railroad gross revenues in September were increased because of the improvement in freight traffic, while net railway operating income, before interest charges, has increased faster and reflects the holding down of transportation, maintenance and other expenses. The spread in gross revenues compared with the same month a year previous was approximately 31 per cent in August, and 21 per cent in September, while the spread in net operating income was narrowed from 50 per cent to only 11 per cent. Quite a number of roads reported an actual increase in net operating income in September compared with a year ago, despite lower gross income, the list including such systems as the following:

Central Railroad of N. J.	Minn., St. P. & S. S. M.
Chicago & Eastern Illinois	N. Y. Central Railroad
Chicago, Mil., St. P. & P.	N. Y., Chicago & St. Louis
Chicago & Northwestern	N. Y., Ontario & Western
Chicago, St. P., M. & Omaha	Pere Marquette Railway
Erie Railroad	Reading Company
Illinois Central Railroad	Southern Railway
Lehigh Valley Railroad	Texas & Pacific Railway
Louisville & Nashville	Wabash Railway

The Wage Question

In the October number of this publication the railroad situation was discussed at some length, and reference was made to the efforts of the railroad companies to obtain a further reduction of wages at the end of the present agreement, February 1, 1933. Special mention was made of the appeal made by the brotherhood chiefs to President Hoover, asking that he use his influence against further wage reductions, on the ground that they would tend to prolong the depression by diminishing the purchasing power of the brotherhood members. This argument was held to be unconvincing, for the reason that it offered no solution of the railroad problem, which demands either an increase of income or a reduction of operating expenses.

The brotherhood chiefs present only a partial view of the case, for they not only ignore the fact that an increase of charges, if effective in raising railroad income, must reduce the purchasing power of the public in like amount, but also ignore the grave probability that in view of the low prices of commodities and the small margin of profit in all business, an increase of transportation charges at this time would intensify the depression and reduce the present volume of railroad traffic, thus lessening employment among railroad men and elsewhere. They also ignore the practical certainty that a further increase of charges at this time, following the increase that took effect last January, would divert more traffic from the rails to the highways and waterways, thereby making the rail problem more difficult. Furthermore, they disregard the fundamental problem, which is to restore normal conditions in industry and trade.

This depression began three years ago, and by now there should be general recognition of the fact that serious derangements exist in the economic system. By this time the natural economic forces would have accomplished a substantial recovery, if their influence had had free play. Something in the nature of a log jam exists in the business stream, and it is of great importance to locate the key logs in the jam. There is reason for believing that the railroad situation is one of them. Furthermore, the high cost of living, notwithstanding the low prices upon food and raw materials, together with the state of unemployment and low aggregate earnings of the whole body of wage workers, notwithstanding high nominal wages, afford a key explanation to the blockade of trade.

It is all very disturbing that with the most strenuous economy only six out of the total of about 150 class I railroads earned their fixed charges in the first six months of this year, that the profits of all business have nearly disappeared, that the country is scarcely maintaining its capital equipment, that notwithstanding the new taxes which went into effect early in July the Federal Treasury is running

behind at a higher rate than a year ago; but there are worse features of the situation than these, as indicated by the Mayor's estimate that nearly one-sixth of the population of New York City will require assistance through the coming Winter.

These conditions must appeal to all our people and should inspire a will to cooperate in whatever action may be necessary to restore the normal state of trade and employment.

It is a fair question, whether in this crisis, the railroad orders have done all that they can afford to do to sustain the industry which gives them employment, or all that is fair and right for them to do to sustain the entire industrial organization, of which they are a vital part. Are they convinced that a reduction of 10 per cent, limited in time to a period that will expire in now three months, is the utmost concession they can make from a wage increase of approximately 157 per cent, (accomplished in a few years under the influence of war and inflation) as their share in a general readjustment of wages and prices which had yielded to them more than a 10 per cent increase in the purchasing power of their wages before their concession was granted?

Are they certain that even from the standpoint of their own interests alone they could afford to see the railroads ruined, with resulting effects upon the country's financial structure and all business, rather than make any further concession? Or do they count upon action by the United States Government, in their behalf, to assume railroad losses and liabilities, along with all its other undertakings for the support of business and employment and the relief of distressed people? If this expectation is the basis of their policy, it is not unreasonable to ask if they have considered how long the public credit would stand up under such demands, in view of the present state of the revenues and present ability of the country to pay taxes or subscribe for bonds? With 40 per cent of their members unemployed the railroad brotherhoods certainly have an interest of their own in the restoration of general prosperity.

Nobody will question that the railroad employes as a body rank high in the citizenry of the country for intelligence and character. They are expected to have as clear an understanding of the mutual obligations which belong to membership in organized society as any other group of members, and to be as responsive to them. They must be given credit for sincerity, but their present attitude can be explained only as resulting from overemphasis upon nominal wage-rates and failure to take account of real wages; also failure to comprehend that their demands tend to derange the entire economic system, delay industrial recovery and prolong and increase the state of unemployment.

In this stand the brotherhood chiefs make common cause with the American Federation of Labor and the labor leaders generally. Again let it be said that the sincerity of these leaders is not questioned, but they may be in error in their analysis of the present problem, and there are good reasons for believing that their wage policy is the principal obstacle to industrial recovery. They all stress the purchasing power of wages as an influence upon consumption, without recognizing that wages enter into industrial costs and prices to consumers. Thus, although wages count both as purchasing power and in costs of living, the labor leaders recognize their influence on only one side of the account. They think of money-wages as original purchasing power, coming from no matter where. The question is worth asking, where do they come from? Is it from the employer? Where does he get them? Tracing through the processes of trade it is evident that they come from the ultimate buyer of the product or service into which the wage worker's labor has entered. And how did this ultimate purchaser get them? Through the purchasing power of some product or service which he has sold on the market. Here is the original source of purchasing power, not in money itself, which is only the medium of transfer or common denominator by which things are valued to each other. In the final analysis all trade is based upon the principle of barter.

Placing all emphasis upon money wages obscures the interdependence of the industries and the fundamental truth that the real compensation of every industrial group for its services comes in the products and services of the other groups. The standard of living is in the products and services which the several groups provide for each other.

The Importance of a Balanced Organization

When the economic system is seen to be what it is, a mutually-dependent, mutually supporting, organization for exchanging services and supplying each other's wants, it should be apparent that the relations within the system are of great importance. Upon the stability of these relations depends the stability of trade, production, employment and consumption. The highest state of prosperity and well being is attained when all parts of this voluntary organization are in such balanced relations that there is full employment for all workers and the varied products and services readily pay for each other, and move steadily into consumption.

In a sound economy the system is regulated automatically by price movements, which tend to distribute the working population into

the occupations as needed to maintain the desired equilibrium in production and prices. If anything occurs to seriously disturb the balanced relations trade necessarily slows down and unemployment results. This is the situation in which this country has been struggling for now nearly three years. Undoubtedly the wants of the people for goods of all kinds are as great as they ever have been and productive capacity is greater than ever before, but price relations have been in such a state of confusion that the volume of trade has fallen off between one-third and one-half. The excess of supplies over market demands has seemed to imply a general state of over-production, but the true explanation is a loss of purchasing power to millions of would-be consumers. This loss is not by reason of a shortage of the money supply or any loss of physical wealth, but is due to the fact that the different commodities and services are not being valued to each other on the same terms as they were a few years ago. If the former price relations were restored the exchanges would soon be flowing as they were then.

In a state of general disorganization such as has existed in these years since 1929 almost all business relations are more or less disturbed and many adjustments have to be made. The economic system requires a degree of flexibility, or adaptability, to enable it to carry on in the periods of disturbed relations which come from time to time. There should be some "give" or elasticity in all relations which are subject to the vicissitudes of the business world, to absorb the shocks of changing conditions and maintain a steady flow of the exchanges.

Inflexible Elements in the Economic System

Certain factors in the economic system are more rigid than others. Prices of commodities of current production coming in volume to the markets are constantly changing under the influence of supply and demand. Compensation for personal services is controlled to a considerable degree by custom and bargaining power and changes less readily. Contracts of all kinds extending over years usually are rigid.

The costs of government have a high degree of rigidity, except that they tend to increase, particularly in good times, when people are free with expenditures and not paying much attention to taxes. Moreover the expenditures of governments are chiefly for personal services and interest on borrowed money, costs which are relatively unyielding.

The people have just now waked up to the fact that taxes have become increasingly burdensome because they are taking an increasing share of all incomes. An organization called the National Economy League has been formed to promote a nation-wide popular effort to reduce the costs of government. Admiral Richard E. Byrd has been elected Chairman, and Ex-President Coolidge, Ex-Governor Alfred E. Smith, the honorables Elihu Root, former Secretary of State, and Newton D. Baker, former Secretary of War, General John J. Pershing and Admiral William S. Sims compose the Executive Committee. This Committee, within the past month, has addressed a public letter to the Chairman in which they declare that taxation is now taking approximately one-third of the national income* and that unless the people arouse and take action they "will find themselves in a condition of servitude to an aggregation of organized and selfish minorities." Governor Roosevelt in his speech at Pittsburgh used corresponding figures, viz.: $45,000,000,000 for the national income and $15,000,000,000 for the total expenditures of governments. An outlay of $15,000,000,000 for government was serious enough when the national income was $90,000,000,000, as in 1929, but becomes crushing when total income drops to $45,000,000,000, and this illustrates the effect of any inflexible claim upon a diminishing total of money-income. On the other hand, since all income at last is in mutual services, if all services were rated correspondingly lower in terms of money the actual exchanges need not be so greatly reduced.

Transportation costs are another important claim upon all business and all incomes, like the costs of government having a high degree of rigidity because the expenditures are chiefly in the form of compensation for personal services. Transportation costs stick out like a sore thumb in comparison with the reduced prices of products transported.

Rents have a high degree of rigidity, but dependent in part upon the contract factor in them. Since the war, rents have reflected the high wages which have prevailed in the building trades and building material industries. Construction costs are one of the "key logs" in the jam.

Debts and interest rates on long term indebtedness are an inflexible element in the situation, and a very important one. Debts always have increased importance in a period of reaction, after a boom period has induced a general increase of them. Interest rates in themselves are not inflexible, for market rates are as changeable as any economic factor, but legal contracts to pay money are not easily changed. The subject, which always involves the money question, is too complex for a full discussion here, but reference is made elsewhere to the tendency of interest rates to decline in periods of depression, and so far as the

***By national income is meant aggregate income of all the people.**

debt burden is increased by a fall of commodity prices, the effect always has been temporary. A general and rapid fall of prices always is due to derangements in the economic system which interfere with the normal flow of products into consumption. When order is restored, as it always has been and will be again, prices recover, and the debts are found not to be so crushing as they appeared in the time of panic.

Finally, wages constitute the principal factor in economic relations, because they are the chief item of costs in nearly every industry and therefore the chief factor in the making of prices. The greater part of the aggregate income of all the people of this country is first received as wages and salaries, and subsequently expended for commodities and services. Thus all of these relationships are affected by wage-rates. We have seen that personal compensation in the form of wages and salaries is the principal factor in the costs of government and in the rigidity which characterizes them. There is great popular sentiment against any proposal to reduce wages, and wage rates therefore have a high degree of rigidity. On the other hand, largely because wage rates are so rigid, employment and actual wage-earnings are subject to great fluctuations, and this is one of the chief reasons why depressions sink as deep and last as long as they do. For in a period of depression large numbers of people find their incomes unavoidably reduced, and if the things they would like to buy do not decline in price there must be a drastic reduction in the physical volume of their purchases, and unemployment results on a large scale.

An Effect of the War

The present state of disorder, the worst ever known, is due primarily to the war, which forced many violent changes in industry and trade. It created an unlimited demand for man-power and caused a vast shift of labor into war industries, which was induced by bidding up wages, and of course had an influence upon all wages. Moreover, the cost of living rose rapidly, on account of the extraordinary demands of Europe for foodstuffs and other necessities, and this properly was taken into account in fixing wages.

In all the past, on account of continuing improvement in methods of production, transportation and distribution, wages have normally moved on an upward course, and it has become a habit of mind to expect them to do so. Furthermore, it has become a fixed principle of organized labor never to permit a retrograde movement. With the usual rate of wage advancement this was possible, but the rise from 1915 to 1929 was wholly abnormal, and could not be made in real wages (commodities) out of current production. The country was not creating wealth at that rate, and the attempt to convert these money-(credit-) wages into commodities drove up the cost of living, rendering the nominal wage advance largely fictitious, in the sense that it did not carry any such increase of purchasing power. These wage rates never should have been regarded as other than emergency rates, intended to compensate for the existing depreciation in the purchasing power of money or, in other words, the rising cost of living. They were not effective in increasing real compensation at the time, and the attempt to maintain them later, when they did represent a substantial increase of real compensation, (after the fall of commodities) has upset the equilibrium of all industry and forced millions of wage-workers out of employment. Industrial costs are relatively so high that the products cannot be sold.

The Conflict of Interests

The labor leaders treat the situation as a conflict between employers and wage-workers and denounce the former for seeking wage reductions. This is an inadequate and mistaken view. The responsible head of an industry very properly endeavors to conform to conditions as he meets them, in order to continue doing business and affording employment for his working force. The conflict which develops when the industrial system is thrown out of balance is not primarily between employers and employes, but between different sections of the economic system, over the terms upon which their products shall be exchanged. There is no fundamental conflict of interests, for all of these groups would be best

Index of Hourly Earnings	Base 1914	Year 1929	July 1932
Agricultural Implements	100	235	204
Automobiles	100	239	203
Boots and Shoes	100	235	190
Chemicals	100	251	218
Cotton Goods (Northern Mills)	100	235	195
Electrical Mfg.	100	229	222
Foundries	100	234	193
Furniture	100	235	193
Hardware	100	227	204
Hosiery and Knit Goods	100	277	196
Iron and Steel	100	250	191
Leather	100	240	212
Lumber and Millwork	100	262	184
Machines and Tools	100	217	203
Machinery—Heavy Equipment	100	215	185
Meat Packing	100	247	194
Paint and Varnish	100	202	176
Paper and Pulp	100	233	195
Paper Products	100	283	246
Printing—Book and Job	100	241	230
Printing—News and Mag.	100	231	197
Rubber	100	263	248
Silk	100	245	192
Wool	100	266	198
Simple Average of these Industries	100	237	197
CLASS I RAILROADS	100	251	*231

* June.
Source: National Industrial Conference Board

served by finding a fair basis upon which their products and services could be readily exchanged and enter into use.

The table on the preceding page gives figures showing the rise of wages upon the railroads and in twenty-four leading industries from 1914 to 1920 and their comparative level in the month of July, 1932. The calculation is based upon average wage rates in 1914 as 100, the figures for 1929 and 1932 representing average wages in these years in percentages of 100. Thus, wages in the agricultural implement industry in 1929 were 235 per cent of wages in 1914, or 135 per cent higher, and in 1932, 104 per cent higher.

The following table gives in cents per hour a showing of union wage scales in the principal building trades in 1913 and 1932, with the percentage of increase, as given in the Monthly Labor Review:

Occupation	Cents per Hour Year 1913	May 15, 1932	Per Cent Change
Bricklayers	67.1	130.0	+ 93.7
Building Laborers	29.9	96.6	+223.1
Carpenters	50.1	100.9	+101.4
Cement Finishers	56.5	116.1	+105.5
Inside Wiremen	51.3	121.7	+137.2
Painters	47.1	116.8	+148.0
Plasterers	64.9	129.9	+100.2
Plumbers	59.7	120.5	+101.8
Stonecutters	57.3	119.6	+108.7
Structural-iron workers	60.6	125.3	+106.8

It will be seen that notwithstanding the wage reductions made between 1929 and July, 1932, average rates in the above-named industries, including the railroads, this year are more than 100 per cent above the 1914 level.

The Primary Industries

The primary industries, producing foodstuffs and raw materials, were very much stimulated outside of Europe during the war, to make up for the loss of supplies that had previously come from Russia and Central Europe. Since the war this new production, largely in the United States, Canada, Australia and Argentina, has been maintained and with the recovery and increase of production in Russia and Central Europe, an excess of supplies has resulted, which has broken down prices. It is needless to say that these scattered producers of primary products have no way of controlling the prices of their products as the workers in the highly organized industries are able to control wages. Adjustments in production must be made, but these require time.

The American farmer has been selling his products this year at about one-half the average prices of 1913. In contrast with this the railroad employes have been insisting that they should not be asked to accept wages less than 157 per cent above their wages in 1913. In the principal American industries, as shown above, average wage rates are now about 100 per cent above the 1913 level. An exchange of services on this basis would mean that the farmer must give nearly four times as much of his products for an hour's factory or railroad wage as in 1913. If the actual increase of freight charges or prices of manufactured goods is not as great as this, it is because the managements have been skillful in introducing economies, usually by labor-saving methods, which have reduced labor costs. With this heavy handicap upon him the farmer has had no alternative but to cut his purchases to the lowest possible point, and employment in factories and on railroads was reduced accordingly.

Effects of the Disruption of Prices

While the loss of purchasing power began with the farmers and other producers of primary products, of course it did not end there. For as these consumers, under the pressure of necessity, reduced their purchases of the products and services of the other industries, and the latter cut down their working forces, the purchasing power of these groups also declined. The entire industrial organization slowed down. Economy in expenditures, both involuntary and dictated by prudence, began on a great scale and continues.

It is urged that the remedy for the situation is to cease reducing wages and promptly restore those which have been reduced. If everybody was a wage-worker, and there was any assurance that all employers were in position to follow this advice, there might seem to be some plausibility in the proposal, but the census figures showing the principal occupational divisions of the gainfully employed population, which were given in this publication last month, indicate what may be expected of this policy.

In 1930, of a population of 122,775,000, there were 98,723,000 persons ten years of age or older and of these 48,830,000 in the language of the Census were "gainfully employed." Of these, 10,472,000 were employed in agriculture, of whom 6,079,000 were owners, tenants or managers, 2,733,000 were hired employes and 1,600,000 were unpaid members of the resident families. There were 9,550,000 operatives and laborers employed for hire in all the manufacturing establishments and 1,072,000 on the steam railroads, these two groups together numbering about the same as the "gainfully employed" upon farms. Forty-four per cent of the entire population lived either outside of incorporated towns and cities or in towns of less than 2,500 people, where all incomes are largely dependent upon farm prosperity. The total number of employes engaged in operating steam railroad trains, which would include the brotherhoods whose wages are now under discussion, was 456,000 and the total member-

ship of the American Federation of Labor is less than 3,000,000. Any one can make his own estimate of how many of the members of these groups, and how many of the remaining gainfully employed, would be likely to have their incomes increased as the result of even the most effective wage-lifting movement that could be organized under present conditions. It is then to be considered that whatever might be thus added to the purchasing power of the recipients must be subtracted from the purchasing power of the whole population, including the farmers and all others whose purchasing power is already below normal, after which he may draw his own conclusions. For there is no way of increasing the income of any section of the population except either through an increased production of wealth within itself or by a transfer of income from other sections of the population.

Present State of the Industries

We referred last month to the appeal of the anthracite coal miners for lower freight rates on coal in order that the price of coal might be reduced to consumers; also to the protests of both miners and railroad employes that they cannot afford to accept lower wages because they have so much lost time. This is the common report from the industries—that existing wage-rates do not produce satisfactory results in the pay envelopes, and therefore the rates must not be reduced. It is evident, however, that these high rates, although ineffectual in producing high wages in the pay envelope, are effectual in making high costs of production and high costs of living; effectual also in reducing consumption, which means reducing the general standard of living. The conclusion appears to be inevitable that the wage-paying industries are on an artificial and uneconomic basis, suffering an enormous waste in the idleness of both labor and capital, causing living costs to be 35 per cent above the 1913 level, while wage scales which are nominally very high in comparison with those of 1913 produce a smaller aggregate of actual wage payments. The explanation is to be found in the unbalanced state of industry, which prevents the normal flow of trade.

A Remedy for Unemployment

Numerous proposals have been offered for dealing with the unemployment problem. There are plans for prevention by some kind of authoritative regulation of industry, for "making" work by public expenditures, and for supporting the unemployed by various schemes, ranging from a tax on industry for insurance to a direct dole from the public treasury. Professor Frank D. Graham, of the Department of Economics, Princeton University, has written a book on the subject* in which he emphasizes employment as the only real remedy, and his book is interesting not only for his plan for providing employment without resorting to the public treasuries but for his comments upon proposals which have had common currency. In the extracts given below, the black letters repeat the emphasis which he gives with italics:

> We have heard it said, with much emphasis of late, that the cure for unemployment is work. This is profoundly true and worthy of all acceptation. The sole problem, therefore, is how that work is to be provided. To solve the problem of providing work is to dispose immediately of the whole question of "relief" by unemployment insurance or otherwise. There can be little doubt that unemployment insurance by enabling the worker to hold out against wage reductions which, in given circumstances, may be essential to the prosperity of industry, can prolong indefinitely the evil the insurance is designed to combat. Unemployment insurance, moreover, even if it had no such ulterior results, would be merely soothing syrup without any therapeutic value. It would, of course, distribute losses, but it is extremely doubtful whether, even in its most perfect form, it could materially diminish the losses it is designed to spread. The same arguments apply to working under any form of short-time.

Recognizing the weakness of insurance plans, Professor Graham says the only alternative to those or resort to charity relief is in opportunity for employment, or as he puts it "employment assurance." Quoting further:

> To provide such assurance is the aim of those who talk glibly about a planned economy. The idea of a planned economy is superficially attractive and we could, no doubt, eliminate some persistent, as contrasted with cyclical, economic maladjustments, if we would exert a little collective forethought. * * * It may, I think, be stated categorically that, with our present knowledge, no "plan" short of that now in effect in Russia, would prove more than very mildly efficacious in preventing business depressions. The great virtue of our existing economic system, moreover, is precisely its lack of conscious, collective planning; its reliance on automatic forces to promote economic ends; its avoidance of regimentation. The freedom of enterprise (and of choice) on which it is based, restricted though it may now be, is a precious possession not lightly to be thrown away, and it has never been shown that the stimulus to progress which it provides can be matched by any possible alternative system. * * * We should not, therefore, deal with unemployment by scrapping the present system of automatic direction in favor of a so-called foresighted guidance the results of which are dubious, to say the least.

After this side-swipe at the schemes for regulating industry, Professor Graham describes the immediate cause of unemployment. He says:

> The mainspring of economic activity in our present system is profits or, if you like, a prospective positive return to the entrepreneur. Now, from the social as well as the individual point of view, there are worse things in this world than profits, and one of them is losses. Whenever, from any cause, profits over a wide range of industries turn into losses we are bound, under present conditions, to have unemployment. Profits vanish, at the margin of production, whenever the shares of total final output going to wage-earners, and to interest or rent-receivers, reach 100 per cent of final production. This is most likely

(*) The Abolition of Unemployment; Princeton University Press; $2.

to happen when there is a fall in commodity prices while money costs remain relatively, if not absolutely, fixed, or when they increase. * * *

Until we get such a reversal of the direction of economic forces it is futile to try to persuade, cajole, or compel employers to maintain their previous scale of costs, particularly aggregate wages. When commodity prices have fallen below such costs, employers, under our present system, simply cannot continue production on the old basis. They may easily bankrupt themselves, however, in trying. It is equally futile, so far as the bulk of the population is concerned, to urge freer spending.

The author's reasoning leads him in search of a plan whereby in times like the present, when wages and prices in terms of money are out of adjustment, resort may be had to the principle of barter, as a temporary expedient by which the otherwise unemployed may supply their own needs.

His plan in brief is to have a National Emergency Corporation that would undertake production, presumably of goods for common consumption, by arrangements with owners of existing shop capacity and giving employment to workmen who would accept pay in "consumption certificates," which would represent proportionate shares in the product. The sole purpose would be to enable the unemployed to produce for themselves and each other during the period of derangement which has deprived them of regular jobs, and to thus mitigate the suffering of such periods.

The consumption certificates would be transferable, and presumably have a money value, hence a recipient might convert a portion of his earnings into cash. Presumably the money value of the wage would be less than the union wage, for avowedly it is an emergency plan to provide employment at times when union wages cannot be had for many would-be workers, but there would be no profit on the labor.

Obviously the problem would be to get such a variety of production and services into the system as would enable it to supply at once employment and the essentials of life to the workers who joined it. Practically the scheme seems to contemplate a cooperative, auxiliary, system in connection with the existing system, but operating with a currency of its own.

The plan bears a resemblance to systems that have been proposed for socialistic societies, but Professor Graham does not offer it as a substitute for the existing system or believe that any socialistic system ever can equal the existing industrial system in serviceable results to the entire population. He has in mind only a plan to bridge over a period of maladjustment between money-wages and prices under the present system. When the maladjustments are corrected and the industrial equilibrium is restored, he expects the free, competitive system to be preferred on its merits. It seems obvious, however, that with a little more understanding and cooperation the maladjustments between money-wages and prices might be readily overcome without a supplementary currency.

Professor Graham recognizes that there are other unyielding elements in the present situation besides wages, notably debts and interest charges. The effects of these cannot be wholly overcome, but he urges that if industry can be maintained to the extent of supplying the current consumption wants of the people the hardships of widespread unemployment will be greatly mitigated and the price and debt situation also helped.

He sums up the case as follows:

Part of the vicissitudes of that [the present] system are due, of course, to the laborers' insistence on maintenance of unchanged money wages when prices are falling. Such insistence is based on some sad experiences in situations where the laborer had right on his side but was in so weak a position as not to be able to maintain his ground. There is, indeed, sound reason for his holding out as long as possible. But, if the laborer demands as wages more money than his product will sell for, he simply cannot be employed. The situation may, it is true, so change as to permit such payment in the future. Meantime, under the scheme above proposed he will get what he can earn without derogation from the established wage rate in ordinary industry and therefore without prejudice to his future earnings when profits, under something like full employment by private industry, again emerge from ordinary economic processes. * * * If we were at war we would not tolerate the waste of productive power now involved in unemployment. The present plan is a war against unemployment and its success is purely a matter of fairly simple organization to overcome the existing disequilibrium between commodity prices and money costs of production.

* * * * * * * *

Skepticism might here be pardoned on the ground that the plan above suggested promises too much. Yet no competent economist holds that unemployment is irremediable and all agree that there is no inherent reason why we should not, year in and year out, produce at the full capacity of our population and resources. Failure to do so is conclusive evidence of defective organization.

The foregoing extracts from Professor Graham's description of his plan obviously give only a skeleton of it. His discussion is valuable for its acute analysis of the entire subject.

It cannot be reasonably questioned that the present state of unemployment results from maladjustments in our free economic system. If these were corrected the anomalous situation in which millions of people are suffering for the necessaries of life which exist in abundance would quickly disappear. But they cannot be corrected without the consent and cooperation of every independent factor in the system. His plan undertakes to avoid the controversy over wages in such an emergency by giving the wage-earner literally his proportion of a product produced without profit, until the system finds its equilibrium again.

With reservations as to the practicability of the plan, we recommend Professor Graham's treatment of the subject as an instructive and helpful presentation.

THE NATIONAL CITY BANK OF NEW YORK

Head Office:
55 Wall Street
New York

Capital, Surplus
and Undivided Profits
$206,554,883.25

Condensed Statement of Condition as of September 30, 1932

INCLUDING DOMESTIC AND FOREIGN OFFICES

ASSETS

Cash in Vault and in Federal Reserve Bank	$190,513,013.56	
Due from Banks, Bankers and United States Treasurer	130,501,277.26	$321,014,290.82
Loans, Discounts and Bankers' Acceptances		665,181,883.12
United States Government Bonds and Certificates	$310,373,464.47	
State and Municipal Bonds	31,506,289.95	
Stock in Federal Reserve Bank	6,600,000.00	
Other Bonds and Securities	110,200,747.02	458,680,501.44
Ownership of International Banking Corporation		8,000,000.00
Bank Buildings		60,455,899.83
Items in Transit with Branches		15,244,803.36
Customers' Liability Account of Acceptances		74,272,523.85
Other Assets		7,217,654.14
Total		$1,610,067,556.56

LIABILITIES

Capital	$124,000,000.00	
Surplus	76,000,000.00	
Undivided Profits	6,554,883.25	$206,554,883.25
Reserves for:		
Contingencies		31,072,317.33
Unearned Discount and Other Unearned Income		2,730,041.28
Interest, Taxes, Other Accrued Expenses, Et Cetera		7,785,358.50
Dividend Payable October 1, 1932		3,100,000.00
Liability as Acceptor, Endorser or Maker on Acceptances and Bills		81,552,249.60
Circulation		1,997,610.00
Deposits		1,275,275,096.60
Total		$1,610,067,556.56

Figures of Foreign Offices which are included herein are as of September 24, 1932

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